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14 April 1987

MEMORANDUM FOR: Distribution

SUBJECT: Inter-Agency Meeting

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| TYPE OF MEETING | Economic Policy Council |
| DATE | Wednesday, 15 April 1987 |
| TIME | 1100 |
| PLACE | Roosevelt Room |
| CHAired BY | Baker |
| ATTENDEE(S) (probable) | NIO/Econ |
| SUBJECT/AGENDA | TBD - <i>Japan Semi-Conductors</i> |
| | |
| | |
| PAPERS EXPECTED | N/A |
| INFO RECEIVED | Per Cabinet Affairs, 1000 |

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*Deane Hoffmann
attended*

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The Director of Central Intelligence

Washington, D.C. 20505

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National Intelligence Council

NIC 01712-87
16 April 1987

MEMORANDUM FOR THE RECORD

SUBJECT: EPC Meeting on Japanese Trade Issues, 15 April

1. The EPC agreed unanimously to proceed with trade sanctions against Japan on 17 April because of Japanese failure to make adequate progress on (a) market access for US computer chips, and (b) eliminating the "dumping" of Japanese chips in third country markets. The game plan is to set the stage for a face-saving accommodation when Nakasone comes to town, and, within two weeks or so, to come up with an agreement on which both sides can declare victory.

2. I warned that the Japanese would not be able to adhere strictly to the conditions that the US was now proposing, and that we should be more explicit about the final US position in order for the Intelligence Community to judge whether Japan could deliver.

3. Secretary Baker said he was concerned about the stability of the Japanese government given trade problems, yen appreciation, and budget difficulties. He ordered that the notification of the trade action should be worded very carefully to make it "non-confrontational."

4. Despite these concerns and warnings, all parties continue to agree that the semiconductor case along with intermittent pressure on the yen is necessary to impress the Japanese that a fundamental change in their world view is needed. Baker reinforced this in a speech to the Japan Society yesterday.

5. Baker also warned the group that the results of the EPC and TPRG trade meetings on Japan were being leaked immediately to the Japanese. Baker discussed this privately with me during the meeting. I told Baker that the person responsible was in the USTR's office.

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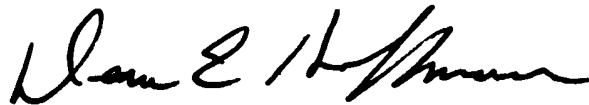
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SUBJECT: EPC Meeting on Japanese Trade Issues, 15 April

6. Lastly, there was a good deal of discussion of the dollar, the US trade deficit, and financial market instability. Those around the table wondered why the press was not taking note of the favorable trends in trade volumes, focusing instead on the large dollar deficits. I asked [REDACTED] OGI, to work with people in EURA and OEA to produce an article on the turnaround on trade volumes for publication in the IEEW.

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Deane E. Hoffmann
National Intelligence Officer for Economics

Attachments:

2 Wall Street Journal articles on Japan, 16 April

cc: ADCI

~~D/Exec Staff~~

[REDACTED]
NIO/EA

Executive Assistant

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THE WALL STREET JOURNAL

16 April 1987

Change 'Essential,' Baker Tells Japan

By PETER T. KILBORN

Special to The New York Times

WASHINGTON, April 15 — Treasury Secretary James A. Baker 3d told Japan tonight that it had reached a "watershed" in its relations with the United States and that "change is essential if good relations and economic growth are to continue."

In a speech to the Japan Society, Mr. Baker cited the spread of protectionist attitudes in the United States and added, "It is surely a reason for special concern that Japan is nearly everyone's principal target."

Mr. Baker's comments came as the falling dollar is squeezing the Japanese economy and President Reagan is preparing to impose punitive tariffs on Japanese goods.

Harshest Comments Yet

The speech was Mr. Baker's longest, most comprehensive and harshest commentary on a country that he — like his counterparts in other nations — has urged to make major policy changes for more than two years.

He said he wanted to make it clear that he seeks no further decline of the dollar against the yen, but he criticized Japan for maintaining policies that contribute to the dollar's decline.

Baker said that Japan does not live up to its promises.

Seeking to dispel speculation that he seeks a lower value for the dollar, Mr. Baker said, "Let me make one point clear: A further decline of the dollar against the other main non-dollar currencies could very well be counterproductive to our goal of higher growth in those countries."

Alleges Unmet Promises

Mr. Baker asked Japan to share leadership of the world economy with the United States, and for the first time he invoked a charge common among other critics, that Japan does not live up to its promises.

He cited the report of a high-level Japanese commission that last year called for a "historical transformation" in the economic policies that have made Japan dependent on exports for growth. Prime Minister Yasuhiro Nakasone endorsed the report, and Reagan Administration officials have cited it as evidence of the emergence of a new Japan.

"Yet a year later," Mr. Baker said, "I think it's fair to say that those words have also not had much effect. Those words — and specific measures to sustain them — are not yet Government policy."

Mr. Baker devoted the body of his remarks to American relations with Japan, and these, he said, were turning sour on both sides. He cited a 93-to-0 Senate vote to retaliate against Japan for reported abuses of a semiconductor trade agreement — the origin of the sanctions that the President is expected to impose on Friday. And he noted Japanese polls showing increased hostility toward the United States.

"Our friendship faces some new and difficult challenges," he said.

Mr. Baker has been urging Japan to reduce taxes and interest rates and adopt other measures that he says would permit it to grow internally, rather than rely on record trade surpluses for growth.

"For all the talk about America's lack of competitiveness," Mr. Baker said, "Japan's economy has actually grown no faster than America's since 1982. And if you consider simply the growth of domestic demand, leaving out exports, America has grown at a rate more than 50 percent faster than Japan. America has created millions of new jobs, while Japan has created very few."

U.S. Given Warning By Japan

By SUSAN CHIRA

Special to The New York Times.

TOKYO, April 15 — Japan formally warned the United States today that an imposition of American tariffs, expected to occur on Friday, would result in a Japanese protest to the international body that governs world trade.

The protest might lead to permission for Japan to impose compensatory tariffs on American goods.

The warning from Japan was made at a meeting in Geneva of the council of the General Agreement on Tariffs and Trade, which governs world trade.

Dispute Over Semiconductors

The United States plans to impose on Friday tariffs on \$300 million of Japanese electronics goods. The dispute centers on American contentions that Japan has failed to fully carry out an agreement on trade in semiconductors.

Takato Ojimi, the director for GATT affairs at Japan's Ministry of International Trade and Industry, said that Japan had told the United States at the Geneva meeting today that Japan believes the tariffs would violate GATT rules.

A GATT tribunal could ask the United States to withdraw the tariffs if it finds a violation of GATT rules and could authorize Japan to impose compensatory tariffs, Mr. Ojimi said.

Officials in Japan are considering a variety of responses to the tariffs ranging from abrogating the semiconductor agreement to offering trade concessions to imposing tariffs without waiting for GATT approval.

Preparing a List

A Japanese trade ministry official, Masaji Yamamoto, said Tuesday that Japan was compiling a list of possible American products on which to impose tariffs. But he added that the possibility of such retaliation was remote — a tacit admission that Japan would certainly be the loser in an all-out trade war with the United States, which last year received 38 percent of Japan's exports.

Nonetheless, it is clear that there are factions within the Government — including some senior officials at the trade ministry — pushing for retaliatory tariffs. Arrayed against them is a more moderate camp,

U.S. Given Warning By Japan

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which includes the foreign ministry as well as key officials in the Prime Minister's office.

Underlying the debate is a conviction that American officials have chosen to get tough on an issue in which they are in the wrong.

The United States contends that, contrary to the agreement, Japanese manufacturers have continued to sell semiconductors below their fair market value and that Japan has failed to import more American-made semiconductor chips. Officials here insist that, while Japan may be open to criticism in some areas, on this issue, it is being attacked unfairly.

One foreign ministry official offered an example of overall Japanese good faith. He said that, despite domestic political pressure, the Government had removed barriers to foreign cigarettes and foreign leather goods, because it was clear that the United States had legitimate grievances concerning those products.

Peril Seen in Inaction

Those in favor of retaliation contend that if Japan does nothing to contest the tariffs, the United States will conclude that threats and sanctions are the way to obtain results in the trade conflict.

Even as officials discuss Japan's response to the United States sanctions, they are working on a package of trade concessions that Prime Minister Yasuhiro Nakasone will bring when he visits the United States at the end of this month.

Running through virtually every discussion of the trade issue here is an insistence on acting logically, on following correct international procedures and on methodically rebutting American charges.

"We can understand the importance of the semiconductor industry for the national security of the United States and the security of the Western alliance," one senior Government official said. "For this purpose, if the United States needs protection, then why not ask Japan frankly to agree, as in the cases of machine tools or steel? Instead, they accuse us of violating the agreement."